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PUBLIC DOCUMENT

Mr. Andrew Stephens
Director
Trade Policy Staff Committee
Office of the United States Trade Representative
600 17th Street, N.W.
Washington, DC 20506

Re: <u>Section 201 Investigation of Steel Mill Products</u>

Dear Mr. Stephens:

We have attached comments of BHP Steel (AIS) Pty, Ltd. and BHP Steel (JLA) Pty, Ltd., of Australia, BHP New Zealand Steel Limited and BHP Steel Americas, Inc. (collectively "BHP") on (1) questions raised by the TPSC regarding BHP's proposal for Section 201 relief on flat carbon and alloy steel products, and (2) the proposals for Section 201 relief on behalf of the U.S steel industry.

BHP stands ready to address in as much detail as possible any additional questions that the TPSC or its member agencies may have.

Sincerely,

John D. Greenwald

Attachment

STEEL SECTION 201 (FLAT PRODUCTS) -- BHP'S COMMENTS ON QUESTIONS RAISED BY THE TPSC AND SUBMISSIONS BY THE DOMESTIC INDUSTRY

A. Answers to TPSC Questions

The TPSC has raised some questions about the specifics of BHP's alternative proposal for tariff rate quotas on feedstock imports for the production of flat-rolled products.

1. Does Section 203 Allow the President to Take Account of Regional Problems in Fashioning Section 201 Relief?

West Coast producers of finished flat-rolled products have no choice but to rely heavily on imported raw material feedstock. The cost of shipping steel from east of the Rockies to the West Coast makes domestic supply of low value feedstock uneconomic under present circumstances and the problem is sure to grow worse once Section 201 restrictions are imposed on imports of finished products. Section 201 import relief will exacerbate the feedstock shortage as domestic mills gain share at the expense of imports in their <u>local</u> markets for <u>finished</u> steel mill products.

Section 203 delegates to the President all the authority he needs to address this regional West Coast problem. Section 203(g)(2) of the Trade Act of 1974 explicitly recognizes the importance of addressing problems related to "imports into a major geographic area" in the context of Section 201 agreements to limit imports. More generally, Section 203(g)(1) of the Trade Act states that the President shall by regulation "provide for the efficient and fair administration of all actions taken for the purpose of providing [Section 201 relief]." It would be plainly "unfair" if Section 201 restrictions on feedstock imports were to cripple West Coast steel mills who are part of the domestic steel industry.

2. Are the Mechanics of Tariff Rate Quotas for Feedstock Workable?

The short answer is "yes." The longer answer is that each U.S. producer of flat-rolled products that relies on imported feedstock knows the specifications (physical and performance characteristics) and volumes of its feedstock imports. Each flat-rolled producer that needs imported feedstock can, therefore, provide precise information for purposes of fashioning narrowly drawn tariff-rate quotas for feedstock, including certification if that is required. Just as the President has, in the past, excluded from Section 201 import relief groups of carefully defined products not produced in the United States, he can, in this case, promulgate narrowly drawn tariff rate quotas for essential feedstock imports. From a technical point of view, administering a tariff-rate feedstock quota for a specific product (whether slab or narrowly defined hot-rolled coil imported for UPI from Posco or imported for Steelscape from BHP) is no more difficult than administering an exclusion for a product not made in the United States. Indeed, a tariff rate quota should be easier to administer because, unlike an exclusion, the feedstock imports subject to the tariff rate quota would be under restraint and, therefore, the scope for "circumvention" of Section 201 relief would be more limited.

3. Why Does BHP Distinguish Between Imports of Feedstock for Flat-Rolled Products and Imports of Feedstock for Other Products?

The key distinction is that domestic flat-rolled producers are not in the business of producing flat-rolled products as feedstock for their direct competitors -- other flat-rolled producers; in contrast, U.S. mills routinely produce and sell plate or hot-rolled coil to unrelated pipe producers and other customers. This difference between feedstock for the production of flat-rolled products and feedstock for other products is both valid and critical.

B. BHP's Comments On U.S. Industry Proposals For Section 201 Relief On Flat-Rolled Steel

The U.S. industry's position on Section 201 relief is very disappointing. Representatives of U.S. Steel, Bethlehem Steel, Nucor and other domestic mills want a prohibitive across-the-board tariff on all flat products without regard to the feedstock needs of U.S. mills that have already restructured by closing inefficient "front-end" capacity and without regard to the effect of their proposed tariff on their customers. At the same time, they resist serious analysis of the economic impact of their proposal and want to avoid meaningful discussion of the central issue of U.S. industry restructuring and positive adjustment to import competition.

1. The Economic "Analysis" Behind the Domestic Industry's Proposal for Relief is Lamentable.

The U.S. mills that support a 40-50 percent ad valorem across-the-board tariff (with a $100 per ton minimum increase) claim that the result would be to

> increase prices in the U.S. market by 6.75 to 8.90 percent, increase domestic revenue by $2.76 billion, and operating income by $1.42 billion [per year].[1/]

These estimates are driven by an econometric model that, like most econometric models, is only as good as the elasticity and other estimates and assumptions fed into it. In this case, the underlying estimates and assumptions are awful:

- The domestic industry model assumes that a 40-50 percent tariff (with a $100 per ton minimum increase) is not prohibitive. In fact, as BHP and others in the business (including Nucor and Bethlehem Steel) know full well, it is.

- The claim that U.S. mills that rely on slab and other feedstock imports would not be harmed because the prices for finished goods would rise is utter nonsense. The domestic industry estimates that slab accounts for 60 percent of the cost of hot-

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[1/] Executive Summary of Comments Regarding the Action the President Should Take Under Section 203(a) of the Trade Act of 1974 Filed on Behalf of Bethlehem Steel Corporation et al. at 3.

rolled coil and estimates a 6-8 percent increase in hot-rolled coil prices after restraints are imposed. By the industry's own calculations, mills that import slab would never be able to "pass through" the added cost of a 40-50 percent tariff on their feedstock.

- There is no effort to account for the benefits of feedstock imports to the domestic industry. Rather, U.S. mills that have restructured their operations around feedstock imports have been treated as if they are not U.S. producers of flat-rolled steel mill products.

- The analysis uses a 2001 base year. What happens to prices if demand during the four year period of relief rises above 2001 recession year levels?

- The analysis appears to assume no serious implications for steel consuming industries; the testimony of these industries before the ITC contradicts this assumption.

We expect that the TPSC agencies will examine the economic "analysis" that stands behind the domestic industry's proposal for relief -- and trust that as its flaws are recognized, the U.S. industry's proposal for relief will be thoroughly discredited.

2. The Domestic Industry Fails to Differentiate Between Imports of Slab and Other Flat-Rolled Products.

A fundamental error in the domestic industry's economic analysis is to assume -- without even an attempt at explanation -- that slab imports are the same as imports of hot-rolled sheet and other flat-rolled products. This assumption ignores the basic fact that slab imports are used as raw materials to produce domestic flat-rolled products. In this regard, slab imports create domestic jobs and help U.S. mills adjust to import competition. Moreover, U.S. mills that rely on imports of slab compete with domestic slab producers in the market for finished flat-rolled products. The reality of this competition renders suspect the domestic slab producers' claim that, once slab prices begin to rise, they will supply an adequate quantity of slab to U.S. mills that lack raw steel making capabilities.

The domestic industry's attempt to lump slab imports together with imports of other flat-rolled products is not rescued by its argument that the business model chosen by domestic importers of slab will lead to the decline of U.S. hot-end capacity.[2/] That claim is completely belied by the record of this investigation. The data accumulated by the U.S. International Trade Commission show a 1 million ton increase in slab imports between 1996 and 2000.[3/] Over the same period, U.S. slab production increased by over 3.35 million tons.[4/] These figures demonstrate that, while slab imports feed companies that do not have sufficient slab making capacity of their own, they are hardly leading to the demise of U.S. hot-end capacity.

3. The Domestic Industry Makes No Serious Attempt to Address a Serious Restructuring Issue.

Section 201 relief is about "positive adjustment" to import competition. The U.S. industry does not make a serious effort to address this serious issue. In a nutshell, the domestic industry's proposed adjustment program can best be described as follows: if restrictions are imposed that increase the U.S. industry's operating income by $1.42 billion per year, the Administration can rely on the industry to spend the money wisely. More than twenty years of hard experience proves otherwise.

In fact, U.S. Steel, Nucor, Bethlehem Steel and the other mills that want a 40-50 percent across-the-board tariff have gone out of their way to discourage serious discussion of industry restructuring. During the U.S. International Trade Commission's hearing, the spokesman for

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2/ See Comments Regarding the Action the President Should Take Under Section 203(a) of the Trade Act of 1974 Filed on Behalf of Bethlehem Steel Corporation et al. at 16-18.

3/ See Staff Report to the International Trade Commission, Certain Steel Products, Inv. No. TA-201-73, USITC Pub. 3479 (Dec. 2001) at Volume II, Table FLAT-4.

4/ Id. at Table FLAT-12.

Wheeling-Pittsburgh made an effort to inject hard truth into the discussion of steel sector relief. Wheeling-Pittsburgh has two blast furnaces; one dates from 1898 and the other from the early 1900s. If Wheeling-Pittsburgh is to survive, it must shut down ancient capacity. In other words, Wheeling-Pittsburgh knows that it cannot continue unless it restructures. To quote the Wheeling-Pittsburgh witness:

> In short, we are not insensitive or uncaring to the problems that exist in the steel industry. By the same token, however, we recognize there is simply no way for U.S. steel companies to continue as they have in the past. We have accepted the following facts. The steel industry is a global industry. We have to lower our capacity by removing old and inefficient facilities, and we will have to adjust our cost of production to deal with the recent drop in prices, which we believe will be a permanent fact of life for our industry. . . .
>
> The best way to adjust to global competition is not to exclude or unfairly or artificially restrict the volume of fairly traded imports, but rather to work with it. Wheeling-Pittsburgh has developed a restructuring plan that is fully supported by our union members for modernizing its facilities, leveraging our world class rolling facilities and which allows for some imported slab as a complement to our domestic production. . . .
>
> Let me conclude with a simple fact. If you exclude slab from the U.S. market or make it prohibitively expensive with tariffs during the period coincidental to our restructuring . . . the company will not be able to adjust to import competition as demanded by the statute and the Administration. Rather, we will continue to trudge along in a cycle of import competition, bankruptcy, layoffs, trade cases and government relief as we have for over 30 years. Surely we can and must do better.[5/]

The spokesman for Wheeling-Pittsburgh should have been applauded. Instead, there was a quick and effective effort to isolate him and challenge the company's adjustment plan.

A number of efficient U.S. mills have already done what Wheeling-Pittsburgh knows it has to do, i.e., they have closed hopelessly inefficient "front-end" facilities and now rely on

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5/ Remedy Tr. at 116, 120 (Bucha).

imported feedstock. They too should be applauded. Instead, the domestic industry is pressing for relief that will actually set back adjustment by subjecting imports of slab and other feedstock to crippling tariffs.

As best we can tell, the domestic industry is asking that the President only pay lip service to the statutory requirements of industry adjustment and restructuring. In this regard, the spirit of the domestic industry's proposal is captured perfectly by the submission on behalf of Nucor and other minimills. Even though Section 203 explicitly directs the President to take account of "positive adjustment" to import competition in fashioning relief, the Nucor submission urges the TPSC to ignore the issue:

> U.S. industry restructuring may be part of the President's overall strategy for dealing with the steel crisis in this country, but the relief here should be focused on the import problem.[6/]

BHP believes that it has made, and can continue to make, a positive contribution to the restructuring plans of U.S. steel mills. About 90 percent of BHP's exports to the United States is feedstock sold to West Coast producers of flat-rolled steel products that do not have any reliable source of domestic supply. After reading the domestic industry's submissions to the TPSC, BHP has come to the sobering conclusion that it cares more about "positive adjustment" of U.S. steel mills than those that purport to speak for the U.S. industry.

6// Comments on What Action the President Should Take Under Section 203 of the Trade Act of 1974 Filed on Behalf of Nucor Corporation et al. at 4.